
# Is insurer responsible for an excess judgment in absence of a policy-limit demand?

## *The courts have sent a mixed message, but here's a look at what is clear today*

**By Arnie Levinson**

The question of whether an insurer can be liable for an excess judgment in the absence of a policy limit demand comes up with surprising frequency in mediation. There is no defining California appellate decision on the issue and there are California cases on both sides of the issue. There surely will be a definite opinion in the not-too-distant future. In the meantime, it is worth looking at the cases we do have – cases on both sides of the issue.

The first case to discuss the issue was *Merritt v. Reserve Ins. Co.,* (1973) 34 Cal.App.3d 858, 877, which stated the generally accepted view that:

> While much remains obscure in this field of the law it is apparent . . . that (1) the legal rules relating to bad faith come into effect only when a conflict of interest develops between the carrier and its insured; (2) a conflict of interest only develops when an offer to settle an excess claim is made within policy limits or when a settlement offer is made in excess of policy limits and the assured is willing and able to pay the excess.

See also *Coe v. State Farm Mutual Automobile Ins. Co*., (1977) 66 Cal.App.3d 981, 996 ("actionable 'bad faith' arises, not from an insurance carrier's obligation to settle, but from an unwarranted failure to accept a reasonable settlement offer.")

### *Boicourt v. Amex Ass. Co.*

Twenty seven years later, that statement was questioned in *Boicourt v. Amex Ass. Co.,* (2000) 78 Cal.App.4th 1390.

In *Boicourt*, the third-party claimant (Boicourt) suffered catastrophic injuries when he was riding in a car with his friend. He asked the insurance company for the insured's policy limits *prior to* filing suit against the insured. The insurance company refused, saying that it had a policy of not disclosing the limits prior to litigation.

Five months into the litigation, the insurer offered up its $100,000 policy limits. Boicourt refused. Boicourt then obtained a stipulated judgment of nearly $3,000,000. (This article does not discuss the enforceability of a stipulated judgment, which is a topic unto its own. See generally, *Pruyn v. Agricultural Ins. Co.,* (1995), 36 Cal.App.4th 500.)

Boicourt then obtained an assignment from the insured for the excess judgment and sued the insurer.

The trial court granted summary judgment because there was never a policy limit demand. The insured said that he could not have made one because he didn't know the limits. However, had he known the limits prior to the litigation, he would have accepted them. The Court found that the insurer had an absolute right to refuse to disclose the policy limits; the insured however, might want the policy limits disclosed so as to encourage a potential settlement prior to litigation. Accordingly, the insurer was required to ask the insured if the insured would like the policy limits disclosed.

The Court of Appeal held that the language in *Merritt,* that bad faith could "only" happen in the face of a policy limit demand, was unnecessary dicta and concluded that:

> Although plaintiff never made a formal settlement offer, such an offer is *not* an absolute prerequisite to a bad-faith action following an excess verdict where, as here, the claimant makes a request for policy limits and the insurer refuses to contact the policyholder about the request. This is so because a blanket rule against precomplaint disclosure of policy limits may create a conflict of interest between the insurer and the insured irrespective of whether the claimant has made a formal settlement offer. Specifically, the insurer saves the administrative costs of having to contact the insure[d] to request authorization to disclose the policy limits, and it also gives the insurer a tactical advantage by forcing the claimant to make prelitigation offers without the benefit of knowing the policy limits or only after incurring the expense of filing a lawsuit and performing some initial discovery.

### *Reid V. Mercury Ins. Co.*

The next case is *Reid v. Mercury Ins. Co.,* (2013) 220 Cal.App.4th 262. The Court identified the issue before it as:

> [A]n insurer's duty to its insured to settle a third party claim within policy limits, when liability is clear and there is a substantial likelihood of a recovery in excess of policy limits. The question is whether the insurer, in the absence of any demand or settlement offer from the third party claimant, must initiate


settlement negotiations or offer its policy limits, and if so how quickly it must do so, to avoid a claim of bad faith failure to settle.

Again, the facts were unusual. The insurer determined immediately that the claim would be far in excess of the policy limits but believed it needed the medical records to confirm that belief. The medical records did not arrive until seven months after the accident. Three months later, the insurer unilaterally offered the policy limits.

The Court held that the insurer did *not* act in bad faith as a matter of law. However, the language of the opinion leaves open the possibility that, under different circumstances, the Court would have permitted a bad faith case to proceed. It too revisited *Merritt* and acknowledged that there were authorities that questioned whether bad faith could occur only in the face of a limits demand.

> But none of these cases suggests that an insurer has a duty to initiate settlement discussions – or an "opportunity to settle" – in the absence of any indication from the injured party that he or she is inclined to settle within policy limits (or at some higher figure where the insured is willing to pay the excess over policy limits).
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> It held,
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> In the absence of a settlement demand or any other manifestation the injured party is interested in settlement, when the insurer has done nothing to foreclose the possibility of settlement, we find there is no liability for bad faith failure to settle.

### *Graciano v. Mercury General Corp.*

*Graciano v. Mercury General Corp.* (2014) 231 Cal.App.4th 414 followed a year later. In this case, the claimant was catastrophically injured when the insured fell asleep at the wheel of his car and hit her. The claimant issued a very quick demand for the $50,000 policy limits to be paid within 10 days. However, there was much confusion over who was actually insured and what policy was in effect. Nonetheless, the insurer scrambled to figure it out and tried unsuccessfully to offer the limits within the 10-day period.

A verdict was later rendered against the insured for over $2 million and the insurer was sued for bad faith. Again, the Court found as a matter of law, that the insurance company did not commit bad faith. "[W]e conclude at a minimum that the insurer *has* satisfied its duty to seek to settle in protection of its insured."

In its discussion, the Court reverted back to the *Merritt* language. Citing *Merritt*, the Court stated, "An insured's claim for bad faith based on an alleged wrongful refusal to settle first requires proof the third party made a reasonable offer to settle the claims against the insured for an amount within the policy limits." (*Id*. at 726.) The Court also interpreted *Reid* as standing for the proposition that "An insured's claim for 'wrongful refusal to settle' cannot be based on his or her insurer's failure to *initiate* settlement overtures with the injured third party." (*Id*. at 427 (Emphasis in original).

The federal courts interpreting California law have also jumped into the fray. *Du v. Allstate Ins. Co*., (9th Cir. 2013) 681 F. 3d 1118 caused quite a stir when it was issued. It purported to interpret an insurer's obligation under Insurance Code section 790.03(h)(5), which states that it is an unfair business practice for an insurer to fail to effectuate prompt, fair, and equitable settlements of claims in which liability has become reasonably clear. *Du* held that this meant that, where liability was clear, an insurer had a duty to offer its policy limits and that failure to do so was bad faith. Many insurers petitioned the Ninth Circuit for a rehearing contending that this holding was unnecessary to the circumstances in *Du* and was poorly thought-out dicta. The Ninth Circuit responded by deleting this portion of the opinion as unnecessary to its holding. (*Du v. Allstate Ins. Co*., (9th Cir. 2013) 697 F. 3d 753.)

### *Travelers Indemnity of Conn. v. Arch Spec. Ins. Co.*

That is essentially where the law stands now based on published opinions. Nonetheless, at least one federal court has tried to figure out what all of this means in an unpublished opinion. *Travelers Indemnity of Conn. v. Arch Spec. Ins. Co.*, (U.S.D.Ct. E.D. Cal. No. 2:11- CV-1601-JQL, Nov. 27 2013) 2013 WL 6198966, grew out of unbelievably tragic circumstances. A truck driver stopped on the side of the road to go to the bathroom. Unbeknown to him, his nine-year old daughter (Diana) also got out of the truck. When the driver returned to his truck, he accidentally ran over his daughter causing her severe injuries.

Diana sued her father and the company which contracted with the father to transport its goods ("FT"). She was eventually awarded $24.5 million. The dispute in *Travelers*, however, was between the two insurance companies who had issued liability policies to FT. Travelers had issued a $2 million primary policy. Arch had issued a $24 million excess policy. Arch claimed that Travelers was responsible for the $22.5 million it was required to pay the girl because Travelers had not followed up on settlement possibilities when it could have. Specifically, Arch claimed that the trial court had determined that FT was liable to Diana. Thereafter, her counsel stated in a mandatory settlement conference statement that the case had a value of $15 million. While this latter statement was admittedly not a demand, Arch claimed that Travelers had failed in its duty to pursue settlement with Diana, when it failed to pursue a settlement within the $15 million.

Travelers moved for summary judgment that it had breached no duty because it was undisputed that no demand – either within or outside the combined policy limits had been made. The Court discussed all of the above authorities and


some additional federal cases. It then arrived at its view of the current state of California law.

> The court also concludes as a matter of law, that under California law, the duty of an insurer to effectuate settlement requires more than merely doing nothing while awaiting a formal written settlement demand. The insurer must act in good faith in response to reasonable opportunities to settle. . . . [A] reasonable jury could find that Diana's MSC statement in August 2008 that "the reasonable value of this case is $15,000,000.00," presented a reasonable opportunity to pursue settlement of the case and that Travelers' failure to pursue settlement discussions at that point constituted bad faith.

## Conclusion

It is undisputed that there are clear authorities holding that there can be no bad faith for an insurer which fails to pursue settlement unless it rejects a reasonable policy limit demand. There are also some courts which have suggested that there may be limited exceptions to this rule. However, no court has thus far affirmed a judgment against an insurer for bad faith in the absence of a policy limit demand. And, except for *Boicourt*, no California Appellate Court has permitted an action to proceed against an insurer absent the rejection of a policy limit demand. Nonetheless, it is safe to say, that there are cases percolating through the appellate system raising these issues and it is likely that we will see more cases discussing this issue.


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